Estate Planning

2004

Estate Planning Objectives

- **Familiarize with estate planning tools and techniques**
- **Understand military survivor benefits**
- **Get you thinking about your individual situations**

Estate Planning *Goals*

- **Taking Care of the Family**
  - Minor (& college-age) children
  - Blended families
- **Disability/Incapacity/End-of-Life planning**
  - Powers of attorney
  - Advance Medical Directive
  - Providing for assisted living
- **Avoiding/Postponing Death Taxes**
  - "Bypass" or "Disclaimer" Trust
  - Leveraging the marital deduction – the QTIP Trust
  - Getting insurance out of the estate – the ILIT
  - Taking advantage of the Gift Tax exclusion
- **Fiduciaries** - Guardians, personal representatives, executors, trustees, and lawyers

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Estate Planning Tool Kit for Military & Family Members

Estate Planning

A continuing process of arranging for the use, conservation, and transfer of one's property/wealth during life and upon death.

Estate Plan

May include one or more of these:

- Will/military testamentary instrument
- Trust
- Life insurance
- Advance Medical Directive/"Will"
- Health Care Power of Attorn
- Durable Power of Attorney
- IRA/TSP/529 Plan beneficiar designation(s)

When Should You Plan?

Now

- While you can
- Before you need

No second chance

What Is "*My Estate*"?

- Gross Estate

- Probate Estate

What Is "*My Gross Estate*"?

Everything I own

- my home, other real estate, bank accounts, investments, retirement benefits, IRAs, TSPs, SGLI/ life insurance, collectibles, personal belongings

What Is *"My Probate Estate"*?

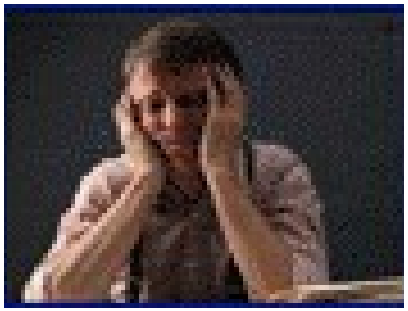
Everything I own – **MAYBE – MAYBE NOT**

- my home, other real estate, bank accounts, investments, retirement benefits, IRAs, TSPs, SGLI/ life insurance, collectibles, personal belongings

Probate

- Legal process
  - Will validated
  - Debts/claims paid
  - Assets gathered & distributed IAW your will (or state intestacy law if no will)
  - Taxes determined & Paid
- Legal way to change title
- Court controls

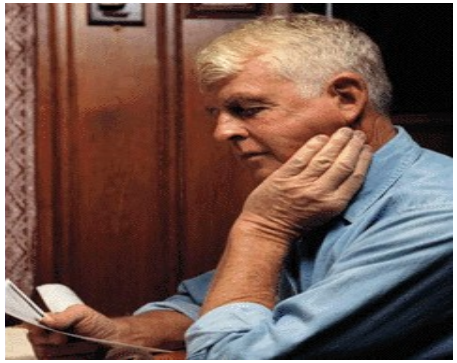
Common Techniques



Do nothing

Joint Ownership

Gifting



Will

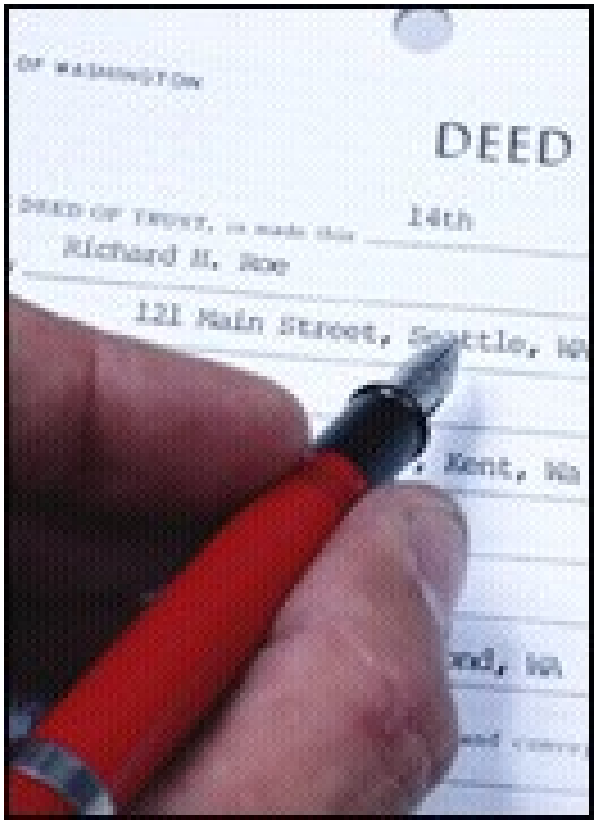
Beneficiary Transfers

Doing Nothing

- At death -
  - Probate
  - Assets distributed under state law
- At incapacity –
  - Court controls assets
- Guardians –
  - Court decides

Property Ownership Methods

- Tenants in Common
- Joint Tenancy with Right of Survivorship
  - Tenancy by the Entirety
- Community Property



JOwRoS – 1st Death

If one dies, survivor becomes sole owner without probate.

Husband dies → Wife Inherits

JOwRoS property not "*probated*" . . . yet

JOwRoS– 2nd Death

What happens when surviving spouse dies?

Spouse dies

Probate

Heirs inherit

JOwRoS - Remarriage

Husband dies → Wife Inherits → **Remarriage**

2nd Spouse dies

Junior disinherited

New spouse inherits *unless* .

Good example of when a trust might be appropriate to ensure Junior is not disinherited

JOwRoS Summarized

1. Postpones probate.
2. Asset title documentation may require change to reflect new ownership.
3. Unintentional disinheriting possible.
4. Incapacity = court in
5. Debts/tax problems.
6. Creditor’s reach.

Beneficiary Transfers

- Governed by state or federal law applicable to “contract” or benefit
- Types
  - Life Insurance
  - IRAs, TSP, 401k, 529 plans
  - Government benefits
- Court involvement *if* beneficiary
  - Incapacitated
  - Dies first or at same time
  - “*My estate*”?
  - Minor

Gifting

- Loss of control
- New owner on transfer
- Can’t “take” asset back
- Useful tool for large estates to remove items from the taxable estate

Wills

- Usual estate plan foundation
- What You Can Do in a Will:
  - Provide for Minor Children (Guardian, Trustee)
  - Designate Distribution of Property/Name Beneficiaries
  - Establish Control Mechanisms for Other Beneficiaries
  - Tax Planning
  - Appoint Who Will Carry Out Your Estate Plan & Wishes
- State Law Governs
  - Validity, Form, Execution, Interpretation

Fiduciaries

- Executors, personal representatives
  - Represent estate for probate, tax purposes, certain elections
  - Extremely broad latitude in most cases, minimal court supervision
  - Whole lotta work! Potential for conflict
  - Some elections (renunciation, QTIP, QDOT) financially crucial
- Trustees
  - Administer trusts, invest, distribute income and corpus, as appropriate, prepare and file necessary legal and tax documents,
- Guardians, conservators, attorneys-in-fact
- And yes, . . . lawyers

Your Fiduciaries

- Select the right person or institution for the job
  - *It is not an honor!*
  - Institutional trustees cost money, but may be worth it in preserving family harmony
  - Beware of multiple fiduciaries—legal gridlock
  - Provide for alternate selection, replacement
- Ensure designated fiduciary knows, understands your wishes, and consents

Wills & Minor Children

- Court
  - Appoints guardian
  - Controls finances
- Child inherits all at legal age (unless trust in will)

Trust

Your TRUSTEE holds property for the benefit of your BENEFICIARY in accordance with the terms of a trust agreement between the TRUSTEE and the GRANTOR (*you*) who established the trust.

[State law controls

Simple Family Trust
Distribution & *Control*

DECEDENT → **TRUSTEE**

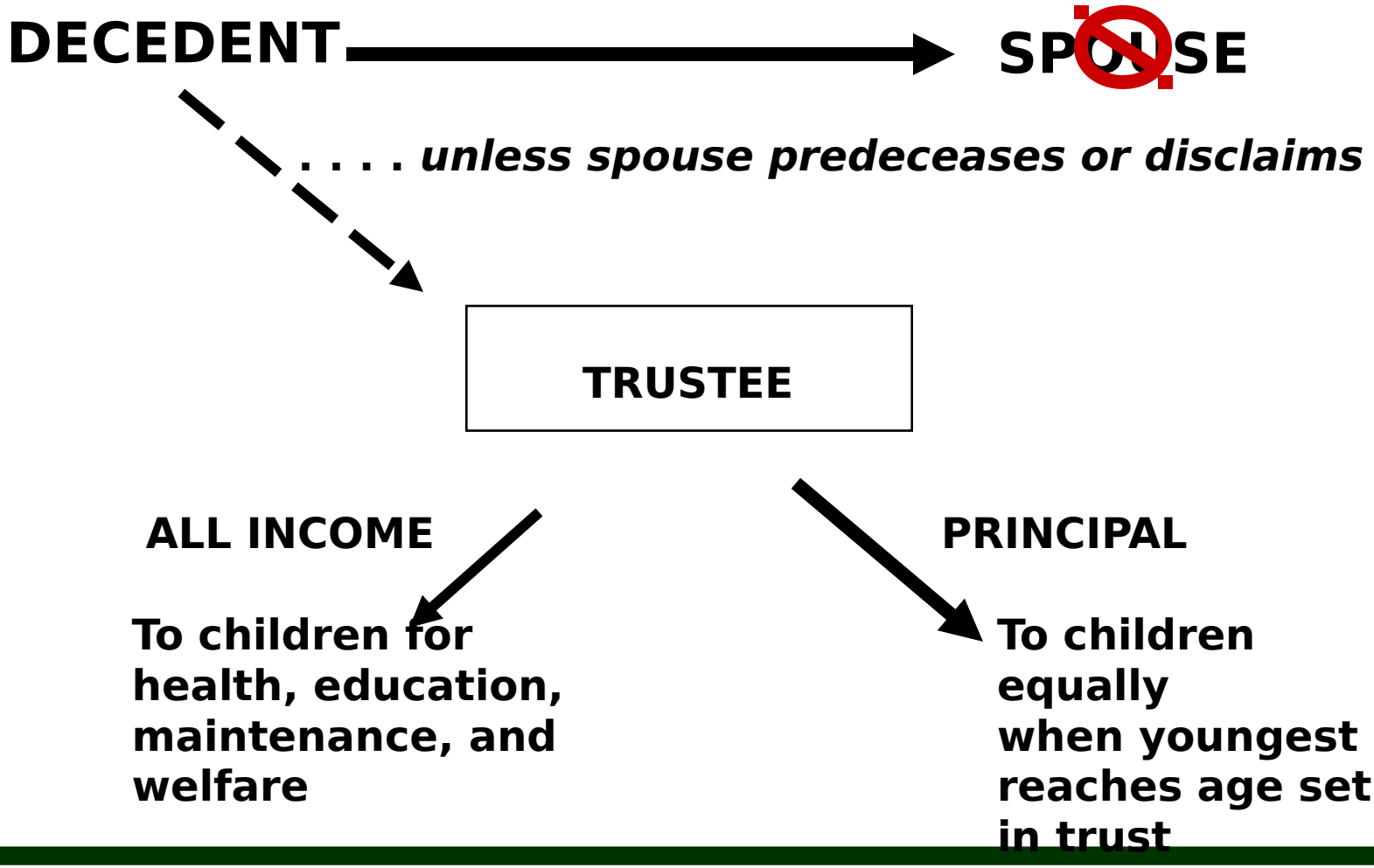
INCOME TO SPOUSE FOR LIFE

SUPPORT OF MINOR CHILDREN

TRUST

OUTRIGHT TO CHILDREN AT SPECIFIED AGE (e.g., 25, 35, 50)

Contingent Trust for Minor Children Distribution & *Control*


DECEDENT
SPOUSE
. . . . unless spouse predeceases or disclaims
TRUSTEE
ALL INCOME
To children for health, education, maintenance, and welfare
PRINCIPAL
To children equally when youngest reaches age set in trust

The *"Blended"* Family

The *"Blended"* Family

For "blended" families, the first-to-die's children may be left out in the cold

- Survivor may change will, remarry, squander estate
- Elective share forecloses disinheriting spouse completely
- Outright bequests to children not eligible for marital deduction, provide no protection to surviving spouse

Estate of LTC Lisa McDonald

- Widowed, two children, marries AD O-4 with two children of his own
  - Substantial estate, based on insurance proceeds from first husband, wise investment strategies
- Mirror-image wills ~ Everything to spouse and then to children (of both spouses) in = shares

***How does first to die ensure equitable treatment of children*?**

One Solution?

- Pre- or Post-nuptial agreement can foreclose use of elective share to frustrate LTC McDonald's intent

- Agreements permit enforcement by third-party beneficiaries (surviving children of first-to-die)

Another Solution
Simple Family Trust
Distribution & *Control*

DECEDENT → **TRUSTEE**

TRUST

INCOME TO SPOUSE FOR LIFE

SUPPORT OF MINOR CHILDREN

→ **OUTRIGHT TO CHILDREN AT SPECIFIED AGE (e.g., 25, 35, 50)**

Trusts

- **Types of trusts:**
  - **Revocable v. Irrevocable**
  - **Inter Vivos Trusts (established during Grantor's life)**
  - **Testamentary Trusts (established at Grantor's death - in Will)**
- **Why establish a trust?**
  - **Control**
  - **Tax minimization**
  - **Privacy/Avoid Probate**

Inter Vivos Trusts

- **“Living Trusts”**
  - **Revocable (*flexible & subject to estate tax*)**
  - **Avoid probate (*good or bad, for assets in the trust*)**
    - **Avoid ancillary probate (*as does JWROS*)**
  - **More private than a probated Will (*generally*)**
  - **Continued management of assets upon Grantor’s incompetence (*in many states, power of attorney is sufficient*)**
  - **Consider/compare cost for similar estate plan in Will (Still must have “pour over” Will if choose to use Living Trust**
  - **Need for asset transfers to trust**

Inter Vivos Trusts

- Other Examples of Inter Vivos Trusts
  - Irrevocable Life Insurance Trusts
  - Grantor Retained Interest Trusts
    - Qualified Personal Residence Trusts
  - Charitable Remainder Trusts

Testamentary Trusts

- **Contingent Trust for Minor Children**
- **Simple Family Trust**
- **Marital Deduction Trust (*Qualified Terminable Interest Property trust (QTIP)*)**
- **Unified Credit Trust *(“By-pass,” “Credit Shelter,” etc.)***

TAX MINIMIZATION
Income Tax Issues

- Maximize beneficiaries' ability to utilize income tax deferral feature of qualified retirement plans.
  - Must consider both estate tax and income tax implications.
- Income taxation of estates, trusts & different individuals.
  - Consider differences in developing estate plan & making transfers.
- Capital gains / step-up in basis

Gross Estate for Estate Tax Purposes

What Is "*My Estate*"?

Everything I own

- my home, other real estate, bank accounts, investments, retirement benefits, IRAs, TSPs, SGLI/ life insurance, collectibles, personal belongings

All property you own at your death.

Valuing Your Estate

• House	$300,000
• Life Insurance	
• SGLI	350,000
• Commercial	500,000 ?
• Investments (e.g., stocks, mutual funds)	150,000
• Bank account	10,000
• Personal property (e.g., car, collections)	50,000
• Retirement benefits (e.g., IRA(s), TSP, pension - SBP)	200,000?
	? Too low?
• Possible inheritance	

Total: $1,560,000

conservative

Estate & Gift Tax Rates

41% on estates over $1,000,00

RISING TO

50% at $3,000,000+

Estate Size	Gross Tax	Credit	Tax Owed*
$1,500,000	555,800	555,800	0
$2,000,000	780,800	555,800	225,000

* Surviving spouse's unlimited marital deduction delays tax on all property passing to surviving spouse.

Estate Tax Minimization

- Basics
  - Taxable estate/unified system/rates
  - Marital deduction
  - Unified credit
  - Gift tax annual exclusion
  - Income tax issues
- Who needs to be concerned?
- Tools & tactics to minimize taxes

Tools & Tactics

- Spend it yourself
- Tax efficient transfers to family & others
  - Lifetime gifts
  - Trusts (testamentary & inter vivos*)
  - Tax efficient distribution in will
- Transfers to charity

*Revocable inter vivos (*living)* trusts have no estate ***tax*** benefit

Estate & Gift Tax Exclusions/Reductions

- Marital deduction
- Unified credit
- Gift tax annual exclusion

Marital Deduction

- Unlimited tax free transfers to a spouse
  - If spouse is U.S. Citizen
  - Lifetime gifts & transfers at death
- Non-U.S. Citizen spouse
  - No unlimited marital deduction
  - Establish qualified domestic trust (QDOT)
  - Gift tax annual exclusion of $110,000 for gifts to spouse who is not a U.S. Citizen

Unified Credit 2004 & Beyond

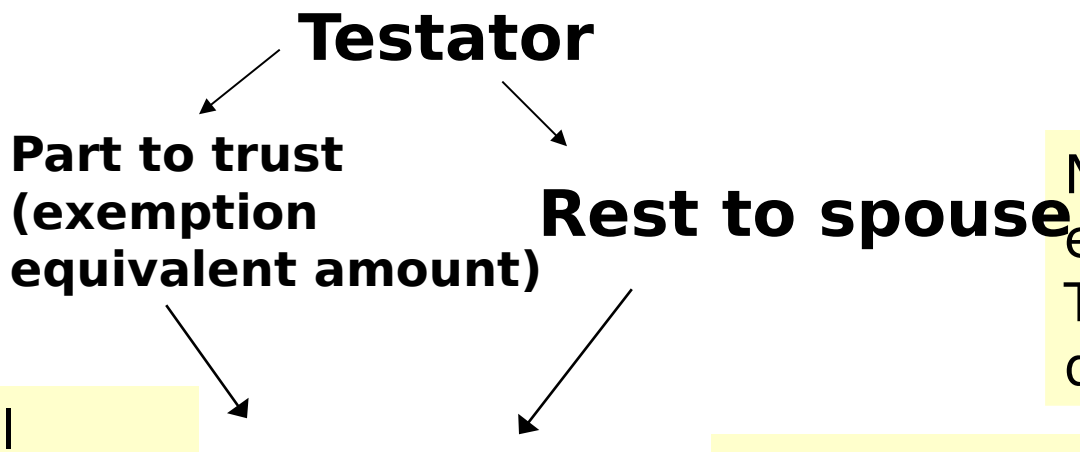
CREDIT =	EXEMPTION
$555,800	**$1,500,000**

Year of Death	**Exempt Amount**
2004 - 2005	1,500,000
2006 - 2008	2,000,000
9	3,500,000
)	ALL
L and after	1,000,000

Gift Tax Annual Exclusion

- Recipient must receive present ownership interest
- Donor can exclude $11,000 per recipient per year ($22,000 split gift)
  - Excess uses unified credit (or is taxed after unified credit exceeded)
  - Indexed for inflation (rounded to ne lowest $1000)

Using By-Pass Credit Shelter Trust in Will


Testator
Part to trust (exemption equivalent amount)
Rest to spouse
No federal estate tax on Testator's death.
No federal estate tax on trust contents. Trust res passes by law.
Beneficiaries (usually children)
Federal estate tax on surviving spouse's death on all in that estate above the exemption equivalent ($1,500,000 in 2004

Unified Credit Shelter Trust

$3,000,000

MARITAL DEDUCTION
NO TAX

UNIFIED CREDIT
NO TAX

$1,500,000
TO SPOUSE

Need not be in
a trust to spouse

SPOUSE'S
UNIFIED CREDIT
NO TAX

$1,500,000
TO TRUST

- **INCOME TO SPOUSE**
- **SPOUSE CAN TAKE UP TO 5% ANNUALLY**
- **ALL IF NEEDED**
- **VERY LIMITED POWER OF APPOINTMENT**

CHILDREN

1ST SPOUSE'S
UNIFIED CREDIT
NO TAX

Using *Disclaimer* Credit Shelter Trust in Will

Testator

To spouse

Disclaims

Creates a trust - *just in case -* preserves Testator's unified credit

No federal estate tax on Testator's death - *unlimited marital*

No federal estate tax on trust contents. Trust res passes by law.

Beneficiaries (usually children)

Federal estate tax on surviving spouse's death on all in that estate above the exemption equivalent ($1,500,000 in 2004

Coordinated Essentials

- Your will
- Durable power of attorney
- Advance medical directive
- Letter of instruction
- Trust*
- Life insurance*
- Contract beneficiary designations*
- Anatomical gift/organ donation*

* As applicable

Durable Power of Attorney

- Survives creator's incapacity
- Allows for asset management of affairs without court supervision
- Springing or non-springing

Health Care Power of Attorney

- Empowers your agent to make health care decisions in event of your incapacity
- State law governs
- Avoids necessity of court proceedings
- Legal effect
  - Holds health care provider harmless
  - Leverages your desires with living advocate
- *Always* springing

Advance Medical Directive

- Control over desired medical treatment
- Directive to physician
- Complements durable power of attorney for health care

"Living Will"

- *Not* a will at all, but directive for end-of-life care
- State law governs enforceability
- As a *general* rule, may direct:
  - *Withholding of life support, heroic measures*
  - *No resuscitation*
  - *Withholding of hydration, nourishment*
  - *Organ donation*
  - *Palliative medicine*

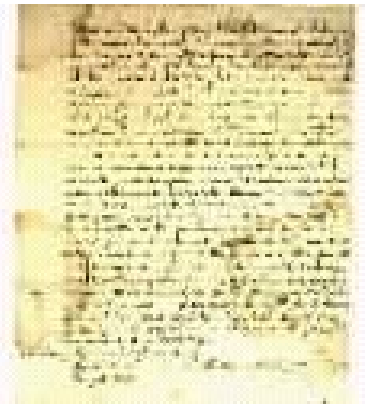
Do You Need Both?

LIVING WILL	DURABLE POA
Directive	Agency
Incapacity Required Required	Incapacity
Terminal Condition Condition	Any Medical

Probably

Letter of Instruction

Compendium of information for your executor/survivors

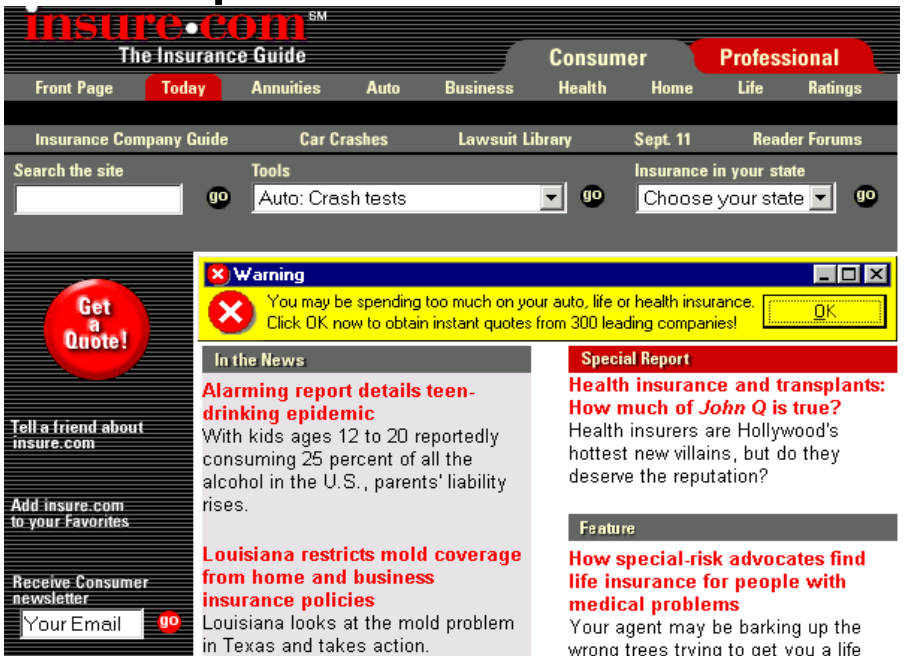


Contents -

- Contacts/notify at death
- Funeral instructions
- Asset inventory & location(s)
- Anatomical gifts (if not on driver’s license)
- Non-binding
- Not a will

Insurance

http://www.insure.com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Auto: Crash tests
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Insurance in your state
Choose your state
go
Get a Quote!
Tell a friend about insure.com
Add insure.com to your Favorites
Receive Consumer newsletter
Your Email
go
Warning
You may be spending too much on your auto, life or health insurance. Click OK now to obtain instant quotes from 300 leading companies!
OK
In the News
Alarming report details teen-drinking epidemic
With kids ages 12 to 20 reportedly consuming 25 percent of all the alcohol in the U.S., parents' liability rises.
Louisiana restricts mold coverage from home and business insurance policies
Louisiana looks at the mold problem in Texas and takes action.
Special Report
Health insurance and transplants: How much of John Q is true?
Health insurers are Hollywood's hottest new villains, but do they deserve the reputation?
Feature
How special-risk advocates find life insurance for people with medical problems
Your agent may be barking up the wrong trees trying to get you a life

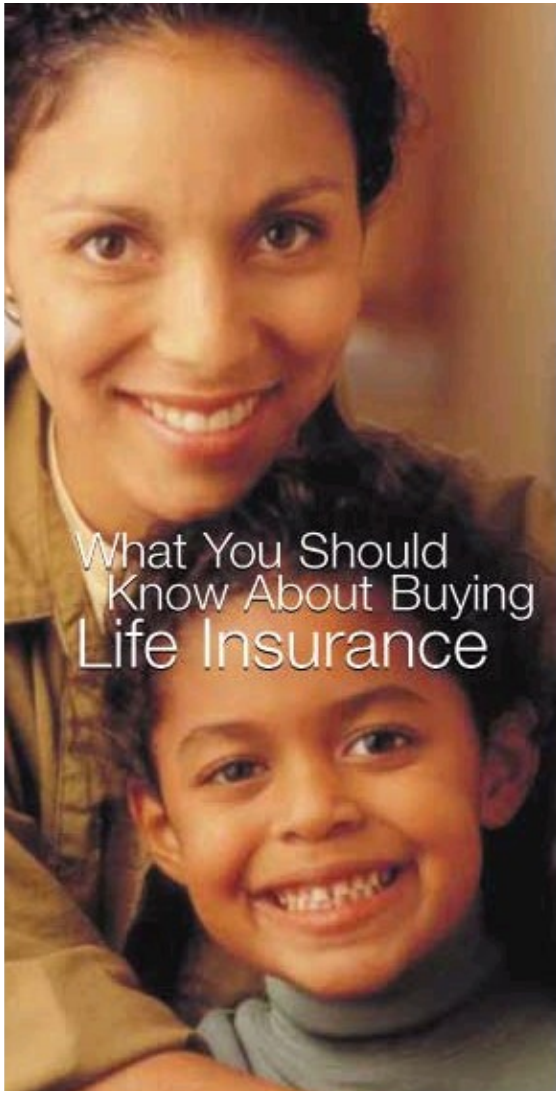
- **Life**
  - Do you need it?
  - How much?
  - What type?
- **Liability**
  - You do need it!
  - Economic decision – how much?
- **Long Term Care**

Do I Need Life Insurance?

- Two purposes of life insurance
  - Protecting family (resource replacement)
  - Liquidity – need cash now!
- **NOT** for investment, please!

Life Insurance Types

- Life
  - Term-pure insurance
  - Hybrid-insurance + forced savings
    - Whole life-guaranteed rate of return
    - Universal life-variety of investments
- *"Buy term, invest the difference"*
  - Assumes discipline



Liability Insurance Limits

- Buy to meet need
- If you want to save, save on comprehensive, collision deductibles
- Umbrella liability policy

LONG-TERM CARE: THE FACTS

- FOR THOSE WHO LIVE TO 65, 1 IN 4 WILL SPEND 1 YEAR OR MORE IN NURSING HOME; 1 IN 11 WILL SPEND 5 YRS OR MORE
- NATIONAL STUDY: 43% OF THOSE 65 IN 1990 WILL ENTER NURSING HOMES DURING LIFETIME
- ANNUAL COST OF NURSING HOME: $38,000
- EXPENSES GENERALLY NOT PAID FOR BY MEDICARE, MEDICARE SUPPLEMENTS OR HEALTH INSURANCE
- MEDICAID WILL COVER LONG-TERM CARE BUT HAS SEVERE INCOME AND

DETERMINING THE NEED FOR LONG-TERM CARE INSURANCE

- AGE
- HEALTH STATUS
- RETIREMENT OBJECTIVES
- INCOME / ASSETS / MEDICAID
- FAMILY
- Monthly Premiums: $117 @ age 50; $235 @ age 65; $571 @age 75

What If I'm Disabled?

- Military Disability Retirement or Separation
- VA Disability Benefits
- Social Security Disability Benefits

Military Disability Benefits

- Medical Retirement *if*
  - 20+ years of service; or . . .
  - 30%+ disability
  - Retired pay or % disabled, whatever is greater (max of 75% base pay)
- Medical Separation *if not retirement eligible*
  - Only 20% or less disability
  - 2 x (monthly base pay) x (years of service)
    - But not more than 12 yrs service

VA Disability Benefits

- VA independently rates disabilit
- Payments based on disability percentage rating
  - Offsets any military disability pay, *but is tax free*
- Other medical, educational benefits may be available

Social Security Disability Benefits

- Tough to qualify
  - Must have contributed to SS five of previous 10 years (20 of last 40 quarters)
    - So severely impaired that cannot perform any substantial gainful activity
    - Disability lasts > 12mos or result in death
  - SS Web site calculator: http://www.ssa.gov/planners/calculators.htm
- Benefits based upon Primary Insurance Amount (PIA)
  - Maximum family benefit is approx. 1.75 PIA

Death Benefits for Survivors of Active Duty Military Members

Survivor Benefits Overview

Monthly Payments	Lump Sum Payments	Other
DIC	SGLI	Burial Reimbursement
SBP	Death Gratuity	Relocation
Social Security	Social Security	Medical Care
DEA	Unpaid Pay	PX/Commissary
	Allowance	Emergency $

***Post*-Retirement Death Benefits**

- SBP (if elected)
  http://www.odcsper.army.mil/default.asp?pageid=16f
- SGLI converted to VGLI (if elected)
  http://www.insurance.va.gov/sglivgli/sglivgli.htm
- Social Security (*only* if minor children) http://www.ssa.gov

The SBP Decision

Run the numbers (rank, years, alternatives, tax bracket)

- Relative health & ages of retiree and beneficiary
- Young or disabled children
  - Payments as long as disabled
  - But, consider impact on Government disability benefits
- Family's need for additional income
- Military member's insurability

Final Thoughts

- Planning is a continuous process
- Plan as a family
- Help raise the awareness of those who work with you

- **Estate Planning Information Center on Legal Services:** http://www.jagcnet.army.mil/legal

Available Services

- Joint Pentagon Legal Office has disbanded
- Army
  - Rosslyn Plaza North – (703) 696-2458
- Navy
  - Room 5E785 – (703) 697-8275
- Air Force
  - Room 5C263 – (703) 697-0413